

# IOWA STATE UNIVERSITY

## Digital Repository

---

Volume 1 | Number 9

Article 2

---

3-16-1990

## Deferral of Federal Disaster Payments

Agricultural Law Digest

Follow this and additional works at: <http://lib.dr.iastate.edu/aglawdigest>



Part of the [Agricultural and Resource Economics Commons](#), [Agricultural Economics Commons](#), [Agriculture Law Commons](#), and the [Public Economics Commons](#)

---

### Recommended Citation

Agricultural Law Digest (1990) "Deferral of Federal Disaster Payments," *Agricultural Law Digest*: Vol. 1: No. 9, Article 2.  
Available at: <http://lib.dr.iastate.edu/aglawdigest/vol1/iss9/2>

This Article is brought to you for free and open access by the Journals at Digital Repository @ Iowa State University. It has been accepted for inclusion in Agricultural Law Digest by an authorized administrator of Digital Repository @ Iowa State University. For more information, please contact [digirep@iastate.edu](mailto:digirep@iastate.edu).

reorganization as to debts arising before confirmation.<sup>20</sup>

- Under Chapter 12 bankruptcy, discharge occurs "as soon as practicable" after completion of payments under the plan.<sup>21</sup> That means, in most cases, discharge in Chapter 12 cases does not occur until three to five years after bankruptcy filing.<sup>22</sup>

- For Chapter 13 bankruptcy, discharge occurs upon completion of payments under the plan.<sup>22</sup>

For those not in bankruptcy, discharge generally occurs at the time of the definitive act discharging the debtor from liability. In some instances, debt was never discharged, only set aside, in which case a claim could be asserted later against the debtor until the statute of limitations runs on the obligation. A 1989 Court of Appeals case indicated that, in a

foreclosure action, for accrual basis taxpayers discharge of indebtedness occurs when all appeals of the action have been exhausted.<sup>23</sup>

**Discharge of indebtedness as gift.** One exception to recognition of discharge of indebtedness as taxable income is where the discharge is intended as a gift.<sup>24</sup> However, that is a concept with very limited applicability except between closely related parties.<sup>25</sup>

**Discharge of indebtedness as self-employment income.** An important issue for farm debtors in recent years is whether discharged of indebtedness is subject to self-employment tax. In a 1976 revenue ruling,<sup>26</sup> cancellation of part of an FmHA emergency loan was considered subject to self-employment tax. The *Farmer's Tax Guide*<sup>27</sup> states that discharge of indebtedness income from farm debt is reported on Schedule F.

That would make the discharged amount subject to self-employment tax. That would seem to be the correct treatment if the debt was related to the operation of a trade or business or business investment in which the taxpayer materially participates. Otherwise, it would seem that discharged debt would not be subject to self-employment tax.

**FmHA position.** In a letter dated May 22, 1989,<sup>28</sup> IRS took the position that debt was considered discharged even though subject to a recapture agreement or a shared appreciation agreement and might later be paid.<sup>29</sup> That position has been criticized by commentators as not reflective of existing law on the subject.<sup>30</sup> This author agrees with that criticism of the IRS position.

## FOOTNOTES

<sup>1</sup> USDA, ERS, Economic Indicators of the Farm Sector, National Financial Summary, 1988, Oct. 1989.

<sup>2</sup> See generally 4 Harl, *Agricultural Law* ch. 39 (1990).

<sup>3</sup> See, e.g., S. 1041, 101st Cong., 1st Sess. (1989) (proposal for relief for gain incurred by insolvent and marginally solvent farmers in connection with debt workouts).

<sup>4</sup> COBRA 1985, Pub. L. 99-272, Sec. 13208, amending I.R.C. § 57(a)(9).

<sup>5</sup> TRA 1986, Pub. L. 99-514, Sec. 405, enacting I.R.C. § 108(g), amended substantially by TAMRA-1988.

<sup>6</sup> See 4 Harl, *supra* note 2, § 39.05[1].

<sup>7</sup> See Treas. Reg. § 1.1011-2(c), Ex. 8.

<sup>8</sup> See *United States v. Kirby Lumber Co.*, 284 U.S. 1 (1931). See also Rev. Rul. 68-523, 1968-2 C.B. 82 (voluntary reconveyance).

<sup>9</sup> *Id.* See I.R.C. § 108.

<sup>10</sup> See Rev. Rul. 68-523, 1968-2 C.B. 82 (amount by which value of property received in involuntary

conveyance exceeds creditor's basis is includible in creditor's gross income).

<sup>11</sup> Rev. Rul. 90-16, I.R.B. 1990-8, 5.

<sup>12</sup> See *Commissioner v. Tufts*, 461 U.S. 300 (1983).

<sup>13</sup> *Id.*

<sup>14</sup> 461 U.S. 300 (1983).

<sup>15</sup> See Treas. Reg. §§ 1.1038-1(d), 1.453-9(a).

<sup>16</sup> 7 C.F.R. § 1421.19(a).

<sup>17</sup> 7 C.F.R. § 1421.23(d).

<sup>18</sup> Ltr. Rul. 8918016, Jan. 31, 1989 (real property of Chapter 7 debtor abandoned to debtor).

<sup>19</sup> *Id.*

<sup>19</sup> Bkrpcy. Rule 4004(a),(c).

<sup>20</sup> 11 U.S.C. § 1141.

<sup>21</sup> 11 U.S.C. § 1228(a).

<sup>22</sup> See 11 U.S.C. § 1222(c) (plans are for three years unless a longer period (not more than two additional years) is approved by the bankruptcy court).

<sup>22</sup> 11 U.S.C. § 1328(a).

<sup>23</sup> *Ryan v. Comm'r*, T.C. Memo. 1988-12, aff'd, 89-1 U.S.T.C. ¶ 9282 (8th Cir. 1989) (accrual basis limited partners realized income from

discharge of indebtedness in taxable year appeal of foreclosure action completed and not year of foreclosure sale).

<sup>24</sup> *Helvering v. American Dental Co.*, 318 U.S. 322 (1943). See *Comm'r v. Jacobson*, 336 U.S. 28 (1949) (repurchase by maker of secured negotiable bonds issued at face value for less than face amount did not involve gift).

<sup>25</sup> *Id.* See *DiLaura v. Comm'r*, T.C. Memo. 1987-291 (no evidence gift intended on discharge of indebtedness).

<sup>26</sup> Rev. Rul. 76-500, 1976-2 C.B. 254.

<sup>27</sup> Pub. 225, Oct. 1989, p. 42.

<sup>28</sup> Letter from Acting Chief Counsel, Peter K. Scott, Internal Revenue Service, to Chet Bailey, Farmer Program Division, Farmers Home Administration.

<sup>29</sup> See Harl, *Farm Income Tax: Annotated Materials*; App. D, Dec. 12, 1989.

<sup>30</sup> See, e.g., Bock & Harris, *Farm Income Tax School Workbook* 209 (Univ. of Illinois, Nov. 1989).

## DEFERRAL OF FEDERAL DISASTER BENEFITS

In the January 19, 1990, *Agricultural Law Digest*, at page 33, we reported that Congress had not acted to permit deferral of benefits under the Disaster Assistance Act of

1989<sup>1</sup> as had been done for the Disaster Assistance Act of 1988.<sup>2</sup> Thus, benefits on the 1989 act received in 1989 were not deferrable to 1990 under the provision permitting crop insurance proceeds (and eligible federal disaster assistance act benefits) to be deferred to the following year by a farmer on the cash method of accounting if, under the taxpayer's

practice, income from sale of the crop would have been reported in the following year.<sup>3</sup>

The statute left little room for argument and states:

"In the case of insurance proceeds received as a result of destruction or damage to crops, a taxpayer reporting on the cash receipts and disbursements method of accounting may elect to include such proceeds in income for the taxable year following the taxable year of destruction or damage, if he establishes that, under his practice, income from such crops would have been reported in a following taxable year. For purposes of the preceding sentence, payments received under The Agricultural Act of 1949, as amended, or title II of the Disaster Assistance Act of 1988, as a result of (1) destruction or damage to crops caused by drought, flood, or any other natural disaster, or (2) the inability to plant crops because of such a natural disaster shall be treated as insurance proceeds received as a result of destruction or damage to crops...."<sup>4</sup>

Notwithstanding the lack of authority in the statute for deferral of disaster payments authorized under such as the Disaster Payment Act of 1989, the Department of the Treasury has now issued temporary regulations permitting deferral in any year if the requirements for deferral are met.<sup>5</sup> Federal disaster payments are treated as crop insurance proceeds for this purpose:

". . . For purposes of this section only, federal payments received as a result of

(i) Destruction or damage to crops caused by drought, floods, or any other natural disaster, or

(ii) The inability to plant crops because of such a natural disaster, shall be treated as insurance proceeds received as a result of destruction or damage to crops. The preceding sentence shall apply to payments which are received by the taxpayer after December 31, 1973."<sup>6</sup>

For those who had already filed their 1989 returns, the election to defer can be shown on an amended return.<sup>7</sup> The election is made by means of a statement attached to the

return (or an amended return) for the taxable year of destruction or damage and is to include the name and address of the taxpayer (or duly authorized representative) along with

- (1) A declaration that the taxpayer's making an election under I.R.C. § 451(d) and Temp. Treas. Reg. § 1.451-6T;
- (2) Identification of the specific crop or crops destroyed or damaged;
- (3) A declaration that under the taxpayer's normal business practice the income derived from the crops that were destroyed or damaged would have been included in the taxpayer's gross income for a taxable year following the taxable year of such destruction or damage;
- (4) The cause of destruction or damage of crops and the date or dates on which the destruction or damage occurred;
- (5) The total amount of payments received from payors (e.g., insurance carriers and government agencies), itemized with respect to each specific crop and with respect to the date each payment was received; and
- (6) The name or names of the payor or payors from whom payments were received.

#### FOOTNOTES

<sup>1</sup> Pub. L. 101-82, 103 Stat. 564 (1989).

<sup>2</sup> Pub. L. 100-387, 102 Stat. 924 (1988).

<sup>3</sup> I.R.C. § 451(d).

<sup>4</sup> *Id.*

<sup>5</sup> Temp. Treas. Reg. § 1.451-6T, 55 Fed. Reg. 7316 (March 1, 1990). IRS also announced that Rev. Rul. 75-36, 1975-1 C.B. 143 will be revoked.

<sup>6</sup> Temp. Treas. Reg. § 1.451-6T(a)(1).

<sup>7</sup> Temp. Treas. Reg. § 1.451-6T(b)(1).

---

## CASES, REGULATIONS AND STATUTES

---

### BANKRUPTCY

#### GENERAL

**ALLOWED CLAIMS.** The debtors had purchased farmland from the creditors, giving cash and promissory notes. After the debtors had filed bankruptcy, the creditors obtained relief from the automatic stay and foreclosed on the farmland. The creditors were the successful bidders for \$140,000. The creditors' own expert witness testified that the land was worth at least \$561,000. The court held that the price paid for the land by the creditors was

unconscionably low and denied their claim for any deficiency against the debtors. ***In re Russell*, 109 B.R. 359 (Bankr. W.D. Ark. 1989).**

**AUTOMATIC STAY.** A tax sale of the debtor's real property in order to pay delinquent ad valorem taxes was a violation of the automatic stay, voiding the sale. ***In re Crosby*, 109 B.R. 195 (Bankr. S.D. Miss. 1989).**

**DISCHARGEABLE DEBT.** A farm debtor was found not to have sold leased cows and used the proceeds for his own debts with fraudulent intent where the owner of the leased cows knew about the sale of the cows and

allowed the debtor to retain the proceeds for several years. The owner of the leased cows had deferred receiving payment for the sale of the cows because of unfavorable income tax consequences. ***Matter of Weber*, 892 F.2d 534 (7th Cir. 1989).**

Debtors had purchased a dairy farm from the creditors, giving a note for most of the purchase price. After several years of timely payments, the debtors abandoned the farm to the creditors and left farming. The creditors foreclosed on the farm and sold it at auction. When the creditors obtained a judgment for the deficiency, the debtors filed bankruptcy. The creditors claimed